

**In the United States Bankruptcy Court  
for the  
Southern District of Georgia  
Statesboro Division**

In the matter of:	)	
	)	Adversary Proceeding
JOHN M. NEIGHBORS	)	
(Chapter 7 Case <u>05-61193</u> )	)	Number <u>06-6008</u>
	)	
<i>Debtor</i>	)	
	)	
	)	
	)	
HOUSEHOLD FINANCIAL	)	
SERVICES, INC.	)	
	)	
<i>Plaintiff</i>	)	
	)	
	)	
v.	)	
	)	
JOHN M. NEIGHBORS	)	
and	)	
BRANCH BANKING &	)	
TRUST COMPANY,	)	
ANNE R. MOORE,	)	
CHAPTER 7 TRUSTEE	)	
	)	
<i>Defendants</i>	)	

**MEMORANDUM AND ORDER  
ON THE CHAPTER 7 TRUSTEE’S MOTION TO SELL REAL PROPERTY**

The Debtor filed a Chapter 7 case on October 14, 2005. He owned a tract of real property at 41 Quail Lake Drive, Swainsboro, Georgia, 30401. Anne R. Moore, the Chapter 7 Trustee, now seeks to sell that property. *See* Dckt. No. 38 (July 24, 2006). Household Financial Services, Inc. (“HFS”) instituted an adversary proceeding against the

Chapter 7 Trustee (hereinafter “Trustee”) on May 15, 2006, seeking injunctive relief to stop the sale and to reinstate a lien that it claimed to hold on that real property. At a September 21, 2006, hearing, the parties agreed to forego any additional discovery or evidentiary hearings and requested that the Court enter a ruling based on the evidence now before it.<sup>1</sup> In light of the issues presented for resolution, I make the following Findings of Fact and Conclusions of Law.

### FINDINGS OF FACT

Upon purchasing the tract of real property in Swainsboro, Georgia, the Debtor executed a note and a security deed (the “First Security Deed”) in the amount of \$280,500.00 to Diversified Capital Corporation of Tennessee (“Diversified”). The First Security Deed was recorded in deed book 102 at pages 374-378 by the clerk’s office of the Superior Court of Emanuel County, Georgia on November 25, 1997. *See* Adv. Proc. 06-6008, Dckt. No. 1, Ex. B (May 15, 2006). Subsequently, the Debtor executed another security deed (the “Second Security Deed”) in favor of Diversified to secure a second note in the amount of \$33,000.00. The Second Security Deed was recorded in deed book 102 at page 379 on November 25, 1997. *See Id.*, Ex. C.

Diversified transferred and assigned the First Security Deed to HFS. *See Id.*, Ex. D. That assignment noted that it was transferring a deed that appeared at deed book 102, page 374. By separate instrument bearing the same date but recorded six years later,

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<sup>1</sup> In a subsequent telephonic conference with counsel on October 3, 2006, I sought the submission of additional relevant evidence, which is now part of the record.

Diversified allegedly attempted to transfer and assign the Second Security Deed to Household Realty Corporation (“HRC”). In that second assignment, however, Diversified assigned the deed appearing at deed book 102, page 374. *See Id.*, Ex. E. The deed book and page numbers of this assignment to HRC are those of the First Security Deed already assigned to HFS, but this assignment recites that the amount of the debt is \$33,000.00, the amount of the Second Security Deed recorded at a different deed book and page number.

On the same date its assignment was recorded, HRC executed a quitclaim deed purporting to cancel the First Security Deed. *See Id.*, Ex. F. The Clerk of the Superior Court of Emanuel County duly stamped the First Security Deed as satisfied and cancelled of record and provided reference to the deed book and page numbers of the cancelling instrument. *See Adv. Proc. 06-6008, Dckt. No. 5, Ex. A (June 12, 2006).*

After the Debtor filed his bankruptcy case, the Trustee discovered the cancellation of the security deeds. She now seeks to sell the Debtor’s property, which is encumbered by another security interest in favor of Branch Banking & Trust Company, and a separate, adjacent tract of land that is encumbered by a deed to secure debt held by Queensboro National Bank. The Trustee contends that the First Security Deed was cancelled of record and that HFS is not entitled to any proceeds to pay off these loans at the time she closes any sale. She argues that HFS should be treated as an unsecured creditor and receive a pro-rata distribution of any proceeds that exceed valid secured claims.

HFS contends that HRC never held an enforceable assignment of the First

Security Deed, which was instead assigned to HFS by Diversified. Therefore, when HRC cancelled the First Security Deed, that cancellation was a nullity. In the alternative, even if the reference in the assignment by Diversified to HRC to the same deed record book and page as the First Security Deed makes that a valid assignment of the First Security Deed, it was a nullity because Diversified had previously transferred and assigned the First Security Deed to HFS. *See* Adv. Proc. 06-6008, Dckt. No. 1, Exs. D & E (May 15, 2006). Therefore, HFS contends, at the time of the second assignment, Diversified no longer had any interest in the First Security Deed that was assignable.

Although the First Security Deed was stamped “satisfied,” HFS contends that a purchaser would have been under a duty to examine the cancellation instrument itself and not rely entirely upon the notation made on the face of the First Security Deed by the Clerk of the Superior Court. This examination would have revealed a discrepancy in the name of HRC, the party purporting to release the deed, and HFS, the holder by assignment of the First Security Deed. Furthermore, the reference in Diversified’s assignment to HRC to the deed record book and page of the First Security Deed, coupled with the amount of the Second Security Deed, at the very least creates an ambiguity as to what was being assigned to HRC. Therefore, HFS claims, reasonable inquiry would have put a bona fide purchaser on notice that HRC’s release might not be enforceable. In addition, HFS asserts that this Court should exercise its equitable jurisdiction to reform the instruments and reinstate the validity of the First Security Deed. HFS cites Decatur Fed. Sav. & Loan v. Gibson, 268 Ga. 362, 489 S.E.2d 820 (1997) and Macleod v. Suntrust Bank Northwest Georgia (In re Henderson), 284 B.R. 515 (Bankr. N.D. Ga. 2002) for the proposition that the cancellation

of a security deed may be revoked.

The Trustee takes the position that as a trustee under the Bankruptcy Code with the strong-arm powers available to a bona fide purchaser, she is entirely protected against HFS's assertion of its right post-petition to reform the First Security Deed because that deed was cancelled of record by the Clerk of the Superior Court of Emanuel County. Furthermore, she contends that HFS has alternative but adequate remedies. These remedies include, but may not be limited to, (1) a suit against the Clerk of the Superior Court for negligence in cancelling the instrument; (2) an action against Diversified for its alleged erroneous assignment to HRC; and (3) an action against HRC because HRC was arguably a stranger to title that filed the instrument with the Clerk of the Superior Court that led to an erroneous cancellation. She asserts that as a bona fide purchaser, she is entitled to rely upon the recorded cancellation and satisfaction of the First Security Deed.

### CONCLUSIONS OF LAW

The Trustee seeks to avoid any secured interest HFS may have in the Debtor's property based upon 11 U.S.C. § 544,<sup>2</sup> which states:

(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

(3) a bona fide purchaser of real property, other than

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<sup>2</sup> Hereinafter, all Section references are to Title 11 of the United States Code.

fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser at the time of the commencement of the case, whether or not such a purchaser exists [and has perfected such transfer].

11 U.S.C. § 544(a)(3).

Under this provision of the Bankruptcy Code, the Trustee “stands in the shoes of a hypothetical bona fide purchaser of real property who might have purchased the property from [the] Debtor at the time of the commencement of the case.” Flatau v. Madonian (In re Sheetex, Inc.), 1999 WL 739628, \*6 (Bankr. M.D. Ga. 1999). As such, the Trustee may avoid any transfer by the Debtor that would not be enforceable against a bona fide purchaser under applicable state law. Whether the Trustee has the status of a bona fide purchaser is determined by Georgia law, which defines a bona fide purchaser as one who purchases for value without actual or constructive notice of the matter at issue. VATACS Group, Inc v. HomeSide Lending, Inc., 276 Ga. App. 386, 391, 623 S.E.2d 534, 539 (2005). The Trustee has the burden of proving that these are appropriate circumstances for her to employ her strong-arm powers under Section 544. *See* Lorance Contracting Co., Inc. v. Mead (In re Woodland Inv. Associates), 95 B.R. 678, 680 (Bankr. W.D. Mo. 1988).

Notice “sufficient to excite attention and put a party on inquiry shall be notice of everything to which it is afterwards found that such inquiry might have led. Ignorance of a fact due to negligence shall be equivalent to knowledge in fixing the rights of parties.” O.C.G.A. § 23-1-17; *see also* Macleod v. Suntrust Bank Northwest Georgia (In re Henderson), 284 B.R. 515, 518 (Bankr. N.D. Ga. 2002)(“It is well settled under Georgia

law that *any circumstance* which would place a man of *ordinary prudence* fully upon his guard, and induce serious inquiry, is sufficient to constitute notice of a prior unrecorded deed.”)(citations and quotations omitted)(emphasis added). A party that purchases land is deemed to have constructive notice of the contents of a recorded instrument within its chain of title. VATACS, 276 Ga. App. at 391, 623 S.E.2d at 539. “Chain of title includes all recorded instruments pertaining to the property that are *executed by an entity holding a recorded interest in the property at the time of the execution of the instrument.*” Id. (emphasis added).

In the present case, the Debtor conveyed an interest in his property to Diversified when he executed the First Security Deed and the Second Security Deed. As a holder of a duly recorded interest in the Debtor’s property, Diversified executed and recorded instruments that were within the chain of title concerning the Debtor’s property, namely the transfer and assignments to HFS and HRC. An examination of the deed book and page numbers used in the transfer and assignments by Diversified to HFS and HRC would have alerted a hypothetical purchaser to the uncertainty concerning the status of both HFS and HRC’s interest in the Debtor’s property.

HRC’s quitclaim release of an instrument assigned to HFS is also sufficient to constitute notice that would “excite attention and put a party on inquiry.” O.C.G.A. § 23-1-17. This situation “would place a man of ordinary prudence upon his guard” and compels this Court to conclude that the Trustee cannot qualify as a bona fide purchaser under Georgia law. In re Sheetex, 1999 WL 739628 at \*7 ; *see also* Watkins v. Hartwell R.R. Co., 278 Ga.

42, 44, 597 S.E.2d 377, 380 (2004)(“One claiming title to lands is chargeable with notice of any matters which appear on the face of any deed forming an *essential link in his chain of title* and of whatever matters he would have learned by any inquiry which the recitals of such deeds made it his duty to pursue.”)(emphasis added). Further inquiry into the validity of the assignments and releases would have revealed that the First Security Deed was arguably still a valid lien on the Debtor’s title. As a result, the Trustee is not a bona fide purchaser without notice and her powers under Section 544(a)(3) do not cut off HFS’s rights to seek reformation of the “cancelled” First Security Deed.<sup>3</sup>

It is undisputed that the assignment of the Second Security Deed from Diversified to HRC mistakenly referenced the same book and page number as the First Security Deed, which had been previously assigned to HFS. Furthermore, HRC’s filing of the quitclaim purporting to cancel and satisfy the First Security Deed was a mistake in that HRC did not have a recorded interest in the First Security Deed when it filed the quitclaim deed. *See* Adv. Proc. 06-6008, Dckt. No. 1, p. 10 (May 15, 2006). The Georgia Supreme Court has stated that a “cancellation obtained by fraud or mistake without payment may itself be canceled by a court of equity.” Decatur Fed. Sav. & Loan v. Gibson, 268 Ga. 362, 364, 489 S.E.2d 820, 822 (1997). As a court of equity, this Court may relieve HFS of Diversified and HRC’s mistake if there is no prejudice to the Debtor and the Trustee. *See Id.* Supplemental evidence provided by HFS demonstrates that there has been no payoff or

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<sup>3</sup> The Trustee relies on the case of Frost v. Gasaway, 229 Ga. 354, 190 S.E.2d 902 (1972). While it is true that the Georgia Supreme Court upheld the enforceability of a superior court clerk’s cancellation of a deed to secure debt, which the concurring opinion termed “fraudulent,” the facts set forth in the opinion do not reveal whether there was anything in the record to alert a title examiner of the irregularity of the cancellation so as to prompt a duty of further inquiry, as there is in the present case. Because of that critical distinction, Frost does not demand the conclusion that the Trustee is a bona fide purchaser under Georgia law.



satisfaction of the First Security Deed and that HFS and HRC are separate and distinct legal entities. *See* Adv. Proc. 06-6008, Dckt. No. 15 (October 6, 2006). The debt remains unpaid, and there is no prejudice in permitting HFS to reclaim the status it held prior to the erroneous filings by Diversified and HRC.

**ORDER**

Pursuant to the foregoing, IT IS THE ORDER OF THIS COURT that the Chapter 7 Trustee's motion to sell the Debtor's property is DENIED. Furthermore, the First Security Deed SHALL BE REFORMED to reflect that the cancellation was in error and that the First Security Deed secures a debt that is still owed to HFS.

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Lamar W. Davis, Jr.  
United States Bankruptcy Judge

Dated at Savannah, Georgia

This \_\_\_\_ day of October, 2006.